

GAO

Report to the Chairman, Subcommittee
on Military Readiness, Committee on
Armed Services, House of
Representatives

February 1999

DOD COMPETITIVE
SOURCING

Questions About Goals,
Pace, and Risks of Key
Reform Initiative



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National Security and
International Affairs Division

B-279771

February 22, 1999

The Honorable Herbert H. Bateman
Chairman, Subcommittee on Military Readiness
Committee on Armed Services
House of Representatives

Dear Mr. Chairman:

The Department of Defense (DOD) is using competitive sourcing¹ through the Office of Management and Budget (OMB) Circular A-76 process as a means of realizing an estimated \$6 billion savings in support costs between fiscal year 1997 and 2003, with over \$2 billion savings expected annually thereafter. You asked that we review the program's progress with an emphasis on the likelihood that it will achieve the estimated savings. Specifically, we (1) identified the competition and savings goals, (2) assessed the accuracy of the savings estimates provided to Congress, and (3) evaluated the adequacy of planning to support the overall program. Our scope and methodology are included in appendix I.

Under A-76, agencies conduct public/private competitions to determine whether the public or private sector will perform selected activities and functions. In conducting competitions for functions being performed in-house, agencies carry out studies to review the current organizational structures, staffing, and operating procedures and to determine the most cost-efficient and cost-effective way of performing the functions.

Results in Brief

DOD has underway an unprecedented program to use competitions to gain economies and efficiencies in its operations and to reduce support costs. While the numbers have evolved over time, as of now, DOD is planning to open over 229,000 government positions to competition within the public and private sectors over the next several years. It estimates \$6 billion cumulative savings between fiscal year 1997 and 2003, and \$2.3 billion in recurring savings each year thereafter, as a result of these efforts.

However, estimates of competitive savings provided to Congress in fiscal year 1998 are overstated, and several issues are likely to reduce the estimated savings, at least in the short term. DOD has not fully calculated either the investment costs associated with undertaking these

¹Throughout this report, we use the term competitions when referring to competitive sourcing governed by the A-76 process.

competitions or the personnel separation costs likely to be associated with implementing them. For example, the Navy is the only service that has included some of these costs to arrive at a net savings figure. Further, there are numerous indications that DOD components have already begun to experience difficulties in launching and completing the competitions within the time frames they initially projected. As a result, the achievement of savings may be delayed. For example, Army headquarters estimated that a study of 4,001 positions at its Training and Doctrine Command would take only 24 months to complete, but the command expects to complete the study in 39 months. As a result, net short-term savings are unlikely to be achieved in the amounts or as quickly as DOD projected. Various officials have expressed concern about the effects of not achieving the expected savings because reductions in future operating budgets have already been planned in anticipation of these savings.

Comprehensive planning to identify specific functions and locations for competition among the services has been limited. Within individual military services, it has largely been up to individual installations or major commands to identify and prioritize specific activities and functions for study and to conduct competitions. The one service that has carried out a comprehensive assessment, the Air Force, has identified a potential shortfall in viable candidates for competition.

Background

Since 1955, the executive branch has encouraged federal agencies to obtain commercially available goods and services from the private sector through competitions when the agencies determined that such action was cost-effective. OMB formalized the policy in OMB Circular A-76, issued in 1966. As part of this process, the government identifies the work to be performed—described in the performance work statement—and prepares an in-house cost estimate, based on its most efficient organization (MEO), and compares it with the best offer from the private sector. Between 1978 and 1994, competition winners were split between the private and public sectors. Appendix II contains a more detailed description of the A-76 process.

Because of lengthy time frames previously required to perform competitive sourcing studies, a provision was included in the DOD Appropriations Act for Fiscal Year 1991 (P.L. 101-511), and in subsequent DOD appropriation acts requiring that single function competitions (under

Circular A-76) be completed within 24 months and multifunction competitions within 48 months.²

Because of administrative and legislative constraints from the late 1980s through 1995, there was a lull—and for some time even a moratorium—on competitions. In 1995, congressional and administration initiatives placed more emphasis on competitive sourcing as a means of achieving greater economies and efficiencies in operations. The Deputy Secretary of Defense in 1995 directed the services to make outsourcing of support activities a priority. Subsequently, DOD placed emphasis on competitions involving both the public and private sectors, known as competitive sourcing.

DOD components identify functions eligible for competitive sourcing studies from a list of commercial activities. Under OMB and DOD guidance, the components must maintain and periodically update their lists of commercial functions, but until fiscal year 1997, they were only required to consider commercial positions that were not inherently governmental in nature.³ In 1997, DOD directed its components to include inherently governmental functions on their lists.

Because of concern over inconsistencies within and among the services in identifying positions eligible for competition, the House National Security Committee in report number 105-132 on H.R. 1119, the Defense Authorization Act for Fiscal Year 1998, directed DOD to develop a uniform set of criteria. DOD's components are currently reviewing which functions performed by DOD personnel are (1) inherently governmental, (2) exempted from competition for national defense reasons, (3) exempted from competition for other reasons, or (4) subject to competitive sourcing competitions. DOD expected to report the results of this reassessment in January 1999.

As we and others have reported, A-76 competitions can be cost-effective.⁴ Data indicates that savings can occur, regardless of whether the

²A single function competition could, for example, involve studying the custodial services at an installation, while a multifunction competition could involve studying both custodial services and refuse collection and disposal services.

³Under the newly enacted Federal Activities Inventory Reform Act of 1998, P.L. 105-270, executive agencies, including DOD, will be required to publish a yearly list of its activities that are not inherently governmental and are performed by a government source. As defined by section 5 of the act, inherently governmental positions generally require the exercise of discretion in applying government authority or the use of value judgments in making decisions for the government.

⁴A complete list of recent GAO reports and testimonies dealing with DOD competitive sourcing is included at the end of this report.

competitions are won by the public or the private sector. Savings may increase if, in accordance with applicable legal standards, multiple functions can be grouped together under a single contract rather than under multiple contracts. Because the average military positions are more costly than their civilian equivalents, greater savings may occur if DOD converts military support positions to government civilian or contractor positions.

While competitions can produce significant savings, caution is needed when estimating the overall magnitude of potential savings. Estimates of savings in the 20- to 30-percent range or higher have been cited in some assessments of previous competitive sourcing studies but often have been based on initial savings estimates from previous competitions, rather than on actual savings over time. DOD has not systematically tracked or updated the savings estimates from competitions. Further, the savings from current competitions may not necessarily match those achieved in competitions completed before defense downsizing—because personnel cuts carried out during downsizing helped streamline organizations and eliminate unneeded positions.

DOD's Competition Study and Savings Goals

DOD has established far greater and more aggressive goals for competitions than in the past. DOD also estimates that the competitions will bring significant cost savings. OMB has recognized DOD as the pacesetter among government agencies in the use of competitions to gain economies and efficiencies in operations and to reduce support costs. However, achieving the goals of an initiative of this magnitude is a significant management challenge.

Study Goals

According to DOD, between 1979 and 1996, it studied over 90,000 positions using the A-76 process. In early 1998, DOD components outlined plans to compete over 225,000 positions between fiscal year 1997 and 2003. The number of positions planned for competition during this period is more than twice the number of positions studied in the previous 17 years. Table 1 summarizes the plans by individual components as of early 1998.

Table 1: Positions Planned for A-76 Competition Announcement

Component	Fiscal year							Total
	1997	1998	1999	2000	2001	2002	2003	
Army	13,173	13,484	13,477	8,146	8,138	0	0	56,418
Navy	10,500	15,000	20,000	20,000	15,000	0	0	80,500
Air Force	13,367 ^a	21,195	18,494	10,107	0	0	0	63,163
Marine Corps	0	800	1,700	1,700	800	0	0	5,000
Defense agencies ^b	0	2,151	6,442	3,002	2,288	6,542	0	20,425
Total	37,040	52,630	60,113	42,955	26,226	6,542	0	225,506

^aIncludes some positions announced in previous years.

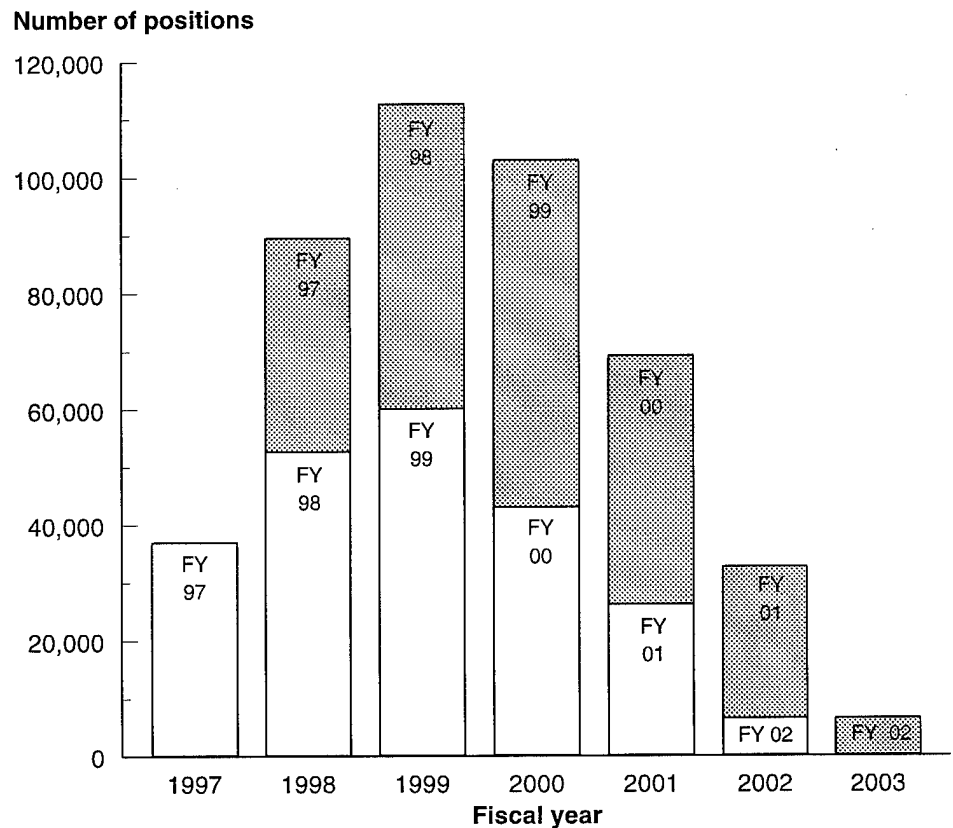
^bFigures shown represent data obtained from the Defense Finance and Accounting Service, Defense Logistics Agency, and Defense Commissary Agency.

Source: Services as of February 1998 and agencies as of May 1998.

According to our analysis, DOD's data indicates that about 79 percent of the positions identified in table 1 are civilian positions, while 21 percent are military positions. Over half of all the military positions to be competed are in the Air Force. The greatest number of positions competed would occur during fiscal years 1999 and 2000. As indicated in figure 1, if DOD components launch the competitions projected for fiscal years 1999 and 2000, and if each competition lasts 24 months, DOD could be competing over 100,000 positions each year during 1999 and 2000.⁵

⁵The DOD budget guidance planning factor for the duration of its A-76 studies is 24 months.

Figure 1: Positions Potentially Under A-76 Competition Between Fiscal Year 1997 and 2003



Note: The dark grey areas in the bars indicate competitions begun in the previous year.

Source: Our calculations based on information from DOD.

Between March 1997 and early 1998, DOD increased the number of positions it plans to compete over the next several years by about 30 percent—from 171,000 to over 225,000. In October 1998, DOD again increased the number of positions expected to be competed to over 237,000 and stretched out the time frame to 2005. However, that figure was recently adjusted to 229,000 by 2005. We were unable to obtain details of how the new numbers would be allocated among the services.

Prior to establishing the competition goal of 229,000 positions, DOD aimed for cumulative savings of about \$6 billion between fiscal years 1997 and 2003. That goal still existed at the time we completed our review and DOD has already begun to reduce future years operating budgets of components in anticipation of these savings and to transfer the expected savings to their research and development and procurement accounts to increase funding for weapon system modernization.

Office of the Secretary of Defense (OSD) guidance projects that components will complete competitions within 2 years and begin transferring funds to higher resource priority budget objectives. According to OSD officials, if the savings do not occur as quickly as planned, the components will have to absorb the shortfalls in their operations and maintenance accounts or shift money back from planned modernization. The Army's competitive sourcing strategic plan, for example, states that if major commands do not achieve programmed savings, they will have to achieve the savings through other efficiencies.

The savings estimates could change. A DOD official told us that, after receiving more detailed information from its components, DOD reduced its projected annual recurring savings as of fiscal year 2004 from \$2.5 billion to \$2.3 billion. This savings figure was still under review when we completed our fieldwork and OSD had not yet decided whether to revise its savings goals or its timetables for achieving them when we completed our review.

Initial Savings Are Likely to Be Less Than Estimated

The projections of competition savings that DOD provided to Congress in fiscal year 1998 appear overstated.⁶ The projections did not adequately consider investment costs related to performing A-76 cost studies. In addition, the competitions will likely take longer to complete than estimated. Both of these factors will affect how quickly DOD components will begin to realize net savings from the competitions. DOD components have expressed concerns about their ability to meet the savings goals. DOD is working to improve these estimates for its fiscal year 2000 budget request.

⁶Our prior reports and testimonies have raised concerns about the services' estimated savings rates from individual competitions; however, for the purposes of this analysis, we accepted DOD's estimates.

Investment Costs Understated

Much like base realignment and closure actions, competitions have up-front investment costs that need to be considered when estimating net savings. In competitions, these investments involve study costs, personnel separation costs, and, in the case of the Army, the costs of substituting civilians for military personnel. Once these investment costs have been offset by program savings, net savings can begin to accrue on an annual recurring basis. However, available information indicates that OSD and its components have not fully and consistently accounted for and deducted these investment costs from their savings projections. This means that DOD will not accrue the estimated initial savings as quickly as projected. However, recurring long-term net savings are potentially significant.

Both OSD and its components made initial assumptions about competition study costs that are understated. While the components are registering concern about these costs, they have not yet developed comprehensive assessments of them.

DOD reported to Congress in April 1998 that the services expected savings of about \$5.8 billion from their competitions and investment costs of \$277 million to conduct the competitions.⁷ Table 2 indicates the savings projected by each service and the identified costs to implement the program.

Table 2: Projected Competition Savings and Investment Costs (fiscal year 1997 to 2003)

Dollars in millions					
	Army	Air Force	Navy	Marine Corps	Total
Investment Costs ^a	\$48	\$0 ^b	\$195	\$34	\$277
Savings	\$1,272	\$1,825 ^c	\$2,533	\$215	\$5,845^d

^aPrimarily for centrally funded contractor support of the competitions.

^bSubsequent to DOD's report, costs of \$53 million were identified by the Air Force.

^cIncludes \$378 million from competitive sourcing efforts at its maintenance depots, which are not governed by OMB Circular A-76.

^dThis report to Congress excluded projected savings from defense agencies that could amount to several hundred million dollars.

Source: Oversight of Outsourced Functions, DOD report to Congress.

⁷The House Committee on Armed Services (formerly known as the National Security Committee), in report number 105-132, cited earlier, requested that DOD report on its oversight of outsourced functions. The savings and investment costs contained in this report, which were based on the fiscal year 1999-2003 Program Objective Memorandum, did not include A-76 initiatives at DOD agencies.

Resource Requirements Appear
Much Greater Than Initially
Projected and Are Not Fully
Identified

DOD's savings projections provided an inconsistent and incomplete picture of A-76 competitive sourcing costs and savings for the period ending in fiscal year 2003. Only the Navy deducted identified investment costs from its net savings estimate. Additionally, available information indicates that DOD and its components understated or later changed their initial estimates of investment costs.

Although the magnitude of the competition program greatly eclipses previous efforts, DOD components have not yet fully identified the resources needed to carry out the competitions. Many components are now projecting that the competitions will likely take much longer and hence require a greater investment of resources than they originally expected and reported to Congress. Many components have noted that this situation is occurring when they have significantly fewer in-house personnel trained to deal with A-76 programs than they had prior to downsizing.

Conducting the competitions may require the use of contractors in addition to existing in-house staff from contracting, personnel, legal, manpower, accounting, internal audit, and the function being studied. To the extent existing in-house resources are limited, if resources need to be shifted to meet new missions, such as performing competitions, other tasks or activities may be delayed or not performed.

DOD initially established a benchmark estimate for competition costs of \$2,000 per position. The benchmark was based on an Air Force analysis of the costs it incurred in performing A-76 studies with in-house personnel. However, that analysis did not include an estimate of costs for developing in-house most efficient organizations, raising concerns that it may have understated the magnitude of the needed resources. In DOD's April 1998 report, the military services estimated different investment costs, some of which were higher than the DOD benchmark. The Air Force did not identify costs because it planned to use only existing in-house staff to perform the work, but will now augment some studies with contractor support. The Navy, however, only identified estimated contractor support costs for conducting the competitions of over \$2,400 per position. The Army based its investment cost estimate only on contractor support costs of \$1,000 for each civilian position, but it did not include funding for competing military positions.⁸ The Marine Corps estimated that its competitions would cost \$6,700 per position and that at least 80 percent of this would fund contractor support.

⁸The Army subsequently revised its cost estimate to \$1,500 per civilian position studied.

Various officials told us that the resource requirements for the studies are much greater than both DOD's \$2,000 benchmark and their service's own initial estimates. For example, officials at one Army major command estimated that they would employ about \$28 million in resources for their competitions—\$4 million for centrally funded contractor support costs and \$24 million for existing in-house staff—to compete 4,000 positions in a multifunction, multilocation study, at least \$7,000 per position. One Navy command estimated that it would incur about \$15 million in costs—\$2.8 million for contractor support and \$12.2 million for existing in-house staff—to compete close to 1,930 positions at various locations, or about \$7,800 per position. A second Navy command estimated that it was spending between \$7,000 and \$9,000 per position—about \$2,000 for centrally funded contractor support and between \$5,000 and \$7,000 for existing in-house staff to conduct competitions. Command officials stated that the command had not received any additional funding for the competitions and that the command would therefore have to provide the additional resources. The large number of competitions planned for the future could necessitate a change in the mix of in-house and contractor personnel required to support the planned competitions. Such changes would affect the extent to which additional funding outlays could be required in addition to those already associated with in-house personnel.

While none of the services has yet fully determined the staff resources necessary to implement its competition program, some service officials have expressed concern about their ability to provide sufficient existing in-house staff as the number of ongoing studies increases and the potential effect on other mission requirements of devoting available resources to meet competition needs. Some officials have already begun to express concern about the adequacy of their resources to initiate and complete ongoing competitions and to deal with other ongoing mission responsibilities. Officials at one Army command stated that they have finite resources to accomplish their overall missions and tasks. If one mission, such as performing competitions, is given command priority, resources are shifted to meet that priority, and other tasks or activities may be delayed or not performed. The large increase in the number of competitions expected to be ongoing in fiscal years 1999 and 2000 is likely to greatly increase resource requirements.

Without allocating sufficient resources to complete the competitions, DOD components may be unable to initiate or complete previously announced competitions within reasonable time frames. The pressure to complete such a large volume of competitions at one time increases the risk of

poorly developed performance work statements, which have historically been cited as a problem area in the competitions. Poor performance work statements require subsequent revisions, reducing the levels of savings from that initially expected.

In July 1998, DOD issued guidance directing the components, when preparing operation and maintenance budget justification material for the fiscal year 2000 defense budget, to (1) report actual and projected competition costs, (2) explain the methodology used to develop the costs, and (3) justify deviations from the average cost of \$2,000 per position. This information should become available when DOD releases its fiscal year 2000 budget request.

Employee Separation Costs Were Not Fully Identified

Except for the Navy, the services understated investment costs because they did not include separation costs for civilian and military DOD employees who lose their jobs as a result of competitions won by the private sector. Implementation costs may also be incurred when in-house organizations win the competitions and the most efficient organizations require a smaller workforce.

Assuming that the private sector continues to win competitions at the historic rate of 50 percent as determined by the Center for Naval Analyses, DOD could transfer work involving more than 100,000 positions to the private sector over the next several years—if it meets its goal of competing over 225,000 positions. Many of the affected civilian government workers could receive some form of separation pay. The Army, for example, estimated an average cost of \$21,000 per person separated. This average covers the costs of voluntary early retirement, voluntary separation incentives, and involuntary separations through reduction-in-force procedures. The Navy estimated an average of \$25,000 per person and the Air Force an average of \$33,000, of which \$25,000 would be funded by headquarters and \$8,000 would be funded by individual commands.

Even if some affected employees fill other positions through DOD's priority placement program, significant numbers of government personnel could still be separated. On the basis of its average separation cost of \$21,000 per employee, the Army's Program Analysis and Evaluation office conservatively programmed separation costs of about \$200 million for only 9,600 employees. The office recognized, however, that the Army would likely separate more personnel. The Air Force programmed \$10 million in civilian separation costs for fiscal year 1999 and programs only 1 year in advance. The Navy did not program any separation costs and will not have

a programming estimate until January 1999 for inclusion in the fiscal year 2000 budget. However, the Navy's competitive sourcing office projected civilian separation costs of \$819 million for 68,250 civilian positions and deducted these costs to reach the savings estimate of \$2.5 billion through fiscal year 2003, that was reported to Congress in 1998.

In July 1998, DOD issued budget guidance directing defense organizations, when preparing their operation and maintenance justification materials for the fiscal year 2000 defense budget, to report transition costs (such as separation pay and voluntary separation incentive pay) they plan to incur and to disclose the methodology and cost categories used to determine those costs.

Replacing Army Military Personnel Will Increase Support Costs

We have previously reported that, on average, the cost of civilian personnel is less than the cost of military personnel. In addition, we have also reported that the conversion of positions from military to civilian (either government or contractor) as part of the competitive sourcing process could save money, assuming that the elimination of the military positions results in corresponding reductions in the authorized end strengths. Such reductions are not expected to be the case for the Army where competitive sourcing eliminates requirements for military positions, without corresponding reductions in authorized end strength.

The Army's 1998 plan called for competing 8,414 military positions.⁹ However, while the Army plans to convert all military positions competed to civilian or contractor positions, it does not expect to take equivalent reductions in military end-strength. Rather, it expects to use military personnel released as a result of the competitions to fill other priorities. Thus, the Army's overall costs will increase by the cost of civilian or contractor personnel selected to replace these military personnel.¹⁰ At the same time, the Army will have to absorb some increases in operations and maintenance costs without additional funding for increased civilian government or contractor costs.

⁹The Army's proposed plan for the fiscal year 2000 defense budget changed the number of military positions to be competed to 6,420.

¹⁰The costs of military positions are funded through military personnel appropriation accounts, whereas funding for costs associated with government civilian or contractor personnel are funded through operation and maintenance appropriation accounts.

Studies May Take Longer Than Planned and Will Likely Delay Savings

As mentioned previously, planned competitions will probably take longer than initially projected. In addition to increasing the study costs, this will also delay net savings. Meanwhile, the services are voicing concerns about their ability to meet the savings targets needed to offset operating budget reductions taken in advance and in anticipation of the savings.

In launching the competition program, DOD and its components made assumptions about the amount of time needed to complete these competitions. DOD's guidance for preparation of the fiscal year 2000 defense budget indicates that competitions should typically take about 24 months to complete. The Army and the Navy initially set more optimistic goals, but many service officials later came to believe that many studies would take longer than 24 months.

The Army's Office of the Assistant Chief of Staff for Installation Management has served as the primary lead for Headquarters, Department of the Army, on issues affecting the implementation of the competitions. This office set competition goals of 13 months for up to 100 positions, 18 months for 101 to 600 positions, and 21 months for over 600 positions. However, Army officials recently expressed some concern about their ability to meet this schedule. For example, the Army's Training and Doctrine Command is conducting a command-wide study of 4,001 positions at 12 installations. This was announced to Congress in November 1996, and Army headquarters projected completion within 24 months. However, because the start of the study was delayed by 6 months and because the competitions cover multiple functions at 12 locations, with phased implementation, the command currently projects completing the last installation by February 2000, or 39 months after it was announced.

Initially, the Navy projected completing its competitions in 12 months, but it revised its assumptions when preparing its 1998 plan because some competitions were taking longer. The 1998 plan estimates that competitions will take between 12 and 36 months, depending on their complexity and including whether they are based on competitions of single or multiple functions.

An Air Force official responsible for program oversight told us that the Air Force currently projects completing competitions within 24 to 48 months and that it expects to meet these time limits.

Components Are Concerned About Meeting Competition and Savings Goals

Since DOD began to emphasize competitions, the goals for the competitions have evolved and grown, even though some DOD components have had difficulties in meeting recent goals for announcing competitions. Some components have expressed concerns about these goals.

OSD officials responsible for monitoring the program consider execution the biggest risk factor. DOD did not have under study all of the positions it planned to study in fiscal years 1997 and 1998 because some competitions that were announced were later canceled, and not all of the remainder were under study. DOD's components planned to announce competitions involving 37,040 positions in fiscal year 1997, but, after cancellations and delayed starts of competitions, they had at most 34,997 positions under study.¹¹ In fiscal year 1998, DOD's components expected to announce competitions involving 52,630 positions, but due to shortfalls by the Navy, the Marine Corps, and the Air Force, they announced plans for competing only 35,710 positions and, after cancellations and delayed starts of competitions, had at most 32,229 positions under study.

According to a Navy official, the Navy was unable to meet its fiscal year 1998 announcement goals because implementing concurrent initiatives such as competitions, regionalization, and consolidation, and meeting mission and mission support requirements stretched available personnel and financial resources. While it did not change the total number of positions it planned to compete between 1997 and 1998, the Navy did change the mix of military and civilian positions and some of its other planning assumptions to meet readiness needs and maintain its projected level of savings. In its fiscal year 1997 plan, the Navy projected competing 30,000 military positions. However, in response to growing concerns about the effect of competitions on the military positions needed to meet sea-shore rotation requirements and other concerns, the Navy in 1998 reduced the number of military positions it would compete by 20,000 and increased the number of civilian positions it planned to compete by the same number. Such a change could mean the potential for significantly less savings since military positions are recognized as relatively more costly to the government.

Officials in the Air Force's competitive sourcing and privatization office said that the Air Force, in developing its fiscal year 2000 budget request, reduced the total number of positions it planned to compete between fiscal year 1998 and 2003 by 23,976 (48 percent). The Air Force did so after

¹¹The Army's and the Air Force's tracking systems are unable to provide the number of positions under study, but Army officials said that revisions to that system should permit that data to be tracked in the future and Air Force officials said that their competitions typically start right after announcement.

completing an analysis and determining that some positions were not viable candidates because some positions were being double counted with ongoing base closure reductions and other positions were not practical to package for competition. However, the officials also said that OSD only agreed to a reduction of about 10,600 positions. Additionally, the Air Force proposed reengineering various functions to achieve additional savings of about \$700 million, about \$116 million more than was planned to have been saved with the competitions.

As previously noted, Marine Corps officials have indicated that they do not believe they can meet their savings goals with the number of positions currently planned for competition. The officials said that the Marine Corps plans to increase the number of positions to be competed from 5,000 to about 6,200.

One difficulty the services are likely to face as they try to identify more competition candidates is the continuing reduction in personnel caused by other ongoing defense reform efforts, cuts mandated by the Quadrennial Defense Review, or other initiatives. Reductions are also planned as a result of legislative requirements. These other ongoing defense reforms could limit the number of positions ultimately available for competition under the competitive sourcing program.

Concerns About the Effects of Failing to Meet Study and Savings Goals

Various service officials pointed to extensive reductions in base operating support budgets in recent years and expressed concern about the additional reductions that are expected in addition to cuts associated with competitions.¹² They expressed concern about their ability to absorb further reductions "out of hide" should they miss their competition savings goals.

Recently, officials in all of the services have voiced concerns about their ability to meet the savings goals established by OSD and the resulting effects, especially considering that the savings have already been taken out of future years' operating budget estimates. For example, an Air Force official told us that the Air Force's major commands will fall short of A-76 savings by about \$141 million in fiscal years 1998 and 1999 and that they will have to absorb these shortfalls. Another Air Force official said that

¹²We previously reported that during fiscal years 1987-1996, total operation and maintenance budget authority declined by 25 percent in real terms, reflecting the overall decline in defense spending. However, annual operation and maintenance obligations for facilities maintenance and repair, excluding family housing, declined by 38 percent on average in real terms during the period. The Army had the steepest decline of all, about 48 percent. See *Defense Infrastructure: Demolition of Unneeded Buildings Can Help Avoid Operating Costs* (GAO/NSIAD-97-125, May 13, 1997).

most major commands are concerned about the effects of funding A-76 competitions and of personnel separation costs on their installations.

Army officials, based on work by the Army Audit Agency, have expressed concern that delayed competition starts could reduce the Army's proposed fiscal year 2000 budgeted gross savings of \$1.6 billion for fiscal years 1999 to 2003 by nearly \$219 million—assuming the competitions are completed within the time frames initially projected, something which the officials consider unlikely. Another Army official indicated that even if the Army can complete all of its targeted competitions by 2003, it may take another 1 to 2 years to implement the results, reduce the workforce, and begin achieving the targeted savings. Additionally, the Army Audit Agency recently stated that the Army's installations and major commands estimate that it will take about 50 percent longer than the time established by the Assistant Chief of Staff for Installation Management to complete the competitions and achieve the expected savings.¹³

Further, an official at the Army's Training and Doctrine Command stated that the command would not meet its \$62-million savings goal in fiscal year 1999 and most of fiscal year 2000. The official stated that the competitions are taking longer than Army headquarters officials projected and that could result in an operations and maintenance funding shortfall.

Officials at the Naval Sea Systems Command stated that they do not believe A-76 competitions alone will be enough for the command to meet its savings goals because there are not enough positions to compete. While the command has a goal to compete 16,415 civilian positions, it had only 7,179 positions categorized as suitable for competition as of October 1998, after its commercial activities inventory review. Since the commercial activities inventory review was still ongoing when we completed our review, we were not able to obtain information on its overall results.

In addition, the Navy's acquisition executive stated in April 1998 that while the Navy would do everything possible to absorb the savings goals, he did not see any way to do this. He established a Process Action Team to review the competitive sourcing program because he believed that the savings were considerably overstated and would result in even more instability in the procurement account.

¹³Observations and Lessons Learned on A-76 Cost Competition Studies, U.S. Army Audit Agency (AA 98-340 Sept. 22, 1998).

Although Marine Corps officials told us that they expected to increase the number of positions to be competed, they also said, at another point, that they could not meet their savings target through A-76 competitions alone. They said they would attempt to make up the shortfall through alternative reform initiatives such as consolidation, regionalization of existing functions, and greater use of technology.

Most Defense Components Lack Detailed Implementation Plans

DOD has provided the needed high-level emphasis, momentum, and sponsorship to energize its competition program and has identified what some have referred to as "stretch goals" in characterizing the larger number of positions to be competed. However, comprehensive planning among the services to identify specific functions and locations for competition has been limited. Detailed planning to implement the program has been largely delegated to components and field activities. These activities are responsible for determining the specific functions that are suitable candidates for competition and whether there are sufficient positions to meet overall competition goals. Such planning is needed to better identify long-term resource needs, especially considering the volume of studies likely to be under way in the future.

To date, the Air Force appears to have performed the most detailed multiyear implementation analysis of its ability to attain its competition goals. The Army, the Navy, and the Marine Corps have not performed a multiyear implementation analysis by function and location, and the Navy and the Marine Corps were unable to provide us with plans of the numbers of positions for competition and projected savings for each major command through fiscal year 2003. The Navy and the Marine Corps are currently developing multiyear competitive sourcing implementation analysis by function and location. The Navy analysis for fiscal years 1999 to 2001 is scheduled to be completed by June 1999 and the Marine Corps plan for fiscal years 2000 to 2002 is expected to be completed by April 1999. According to service officials, some or all of the major commands were given numbers of positions to compete and savings goals, and it is up to them to determine how best to meet the goals.

The Navy started developing a strategic plan for competitions in September 1997, about 2 years after the Chief of Naval Operations revitalized the Navy's competition program. In response to a prior GAO recommendation, the Navy expects to develop a detailed 5-year plan as part of its overall strategy and expects the major commands to develop an execution plan. The Navy expects to have a reasonable and achievable

strategic plan for competitions by early fiscal year 1999. The extent to which this strategic plan will be based on a detailed implementation analysis is unknown at this time.

The Army published a competition strategy in September 1998 but has not conducted a detailed implementation analysis of the program to assess its executability. The strategy lays out a number of high-level goals and identifies ways to meet them. In implementing its strategy, the Army is placing primary responsibility for selecting and prioritizing functions and conducting competitions on the installation commanders. Army officials told us that each year, the major commands develop a plan that identifies the functions the commands will study at their installations that fiscal year. If the major commands do not achieve the programmed savings from competitions, they must achieve the savings through other efficiencies or local personnel management actions. The Army has also established a competitive sourcing and privatization Integrated Process Team and made it responsible for recommending a new management structure to oversee the program and changes to streamline processes. Team officials recommended that the Army develop competition plans for the fiscal year 2001 to 2005 time frame by April 1999. The recommendations were made on November 19, 1998, and are currently awaiting approval from the Army Vice Chief of Staff. The extent to which the competition plans will be based on a detailed implementation analysis is unknown at this time.

OSD, on December 9, 1998, directed each component to develop multiyear competition plans consistent with and presented at the same time as their fiscal year 2001 to 2005 Program Objective Memorandum. OSD directed that these plans should include, by fiscal year, the functions and numbers of positions to be competed.

Conclusions

DOD has established an ambitious competition program as a means of reducing its infrastructure support costs and increasing funding available for modernization and procurement. Establishing realistic competition and savings goals are key to achieving the program's desired results. However, DOD's savings projections have not adequately accounted for the costs of conducting the competitions. These costs could significantly reduce DOD's expected level of savings in the short term. In addition, the planned competitions are likely to take longer than initially projected, further reducing the annual savings that will be realized. Consequently, the estimated savings between fiscal year 1997 and 2003 are overstated. The effects of failing to realize these annual savings could be significant, since

DOD has already reduced future operating budget estimates to take into account the estimated savings.

Also, the number of competitions DOD expects to complete over the next several years continues to increase, even as difficulties in meeting previous goals grow. Service officials are increasingly expressing concern about their ability to meet these targets, especially considering the unprecedented number of competitions that are planned to be ongoing simultaneously in the near future. Finally, we believe there is merit to this concern because most components lack detailed plans and analyses to help determine whether the numbers of positions to be competed would be practical.

Recommendations

We recommend that the Secretary of Defense require the DOD components to assess to what extent available resources are sufficient to execute the numbers of planned competitions within the time frames envisioned and make such adjustments as needed to ensure adequate program execution. In doing so, we also recommend that the Secretary require the components to reexamine and adjust as necessary the competitive sourcing study targets, milestones, expected net short-term savings, and the planned operating budget reductions.

Agency Comments and Our Evaluation

In commenting on a draft of this report, DOD concurred with our conclusions and recommendations (see appendix III). However, the response also indicated that DOD does not believe that its components have completed enough studies since fiscal year 1997 to establish a baseline that would necessitate the reevaluation of competitive sourcing milestones and objectives at this time, as our report recommends. DOD noted that the Deputy Secretary of Defense had proposed a number of initiatives in a December 9, 1998, memorandum to the Defense components that will make better use of existing resources devoted to competitive sourcing studies. However, DOD did not indicate at what point it would establish a new baseline.

We continue to believe that DOD has sufficient reason to reassess the competitive sourcing study targets, milestones, expected short-term savings and planned operating budget reductions now. The issues at hand involve more than the number of competitions completed, they also involve to what extent the planned announcements of competitions have occurred and whether there are sufficient resources to complete them.

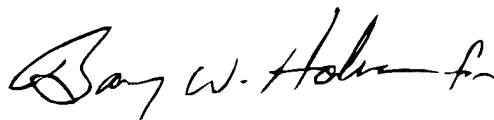
This is of concern especially given the large number of studies planned for announcement in fiscal years 1998 and 1999 and the delays encountered in getting the fiscal year 1998 studies underway. If similar delays are encountered in fiscal year 1999, they could seriously affect future program execution and DOD's ability to achieve results in a timely manner. Accordingly, an important part of any reassessment should also include examining the components' progress in developing detailed implementation plans; such plans will have a direct bearing on resource requirements.

DOD also provided technical comments to the draft, which we have incorporated as appropriate.

We are sending copies of this report to the Chairmen of the Senate Committees on Armed Services and on Appropriations and of the House Committees on Armed Services and on Appropriations; the Secretaries of Defense, the Army, the Air Force, and the Navy; the Commandant of the Marine Corps; and the Director, Office of Management and Budget.

Please contact me at (202) 512-8412 if you or your staff have any questions concerning this report. Major contributors to this report are in appendix IV.

Sincerely yours,

A handwritten signature in black ink, appearing to read "David R. Warren". The signature is fluid and cursive, with a stylized "D" and "W".

David R. Warren, Director
Defense Management Issues

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Abbreviations

CAMIS	Commercial Activities Management Information System
DOD	Department of Defense
FYDP	Future Years Defense Plan
IFB	Invitation for Bid
MEO	most efficient organization
OMB	Office of Management and Budget
OSD	Office of the Secretary of Defense

Scope and Methodology

For this report, we (1) identified the Department of Defense's (DOD) competitive sourcing study and savings goals, (2) assessed the accuracy of the savings estimates provided to Congress, and (3) evaluated the adequacy of program planning to support the overall program.

To determine the Office of the Secretary of Defense's (OSD) process for managing the A-76 savings targets, we met with representatives of the Defense Management Council, including OSD's Office of Program Analysis and Evaluation and the A-76 Task Force in the Office of the Deputy Under Secretary of Defense for Industrial Affairs and Installations.

To identify DOD's competitive sourcing study and savings goals and assess how well investment costs are reflected in the savings estimates, we obtained and analyzed the planning assumptions each military service and OSD used. We did not use the budget justification material on competitive sourcing contained in the 1999 to 2003 Future Years Defense Plan (FYDP) because of certain limitations in the data. Instead, we obtained comprehensive information from each service on the numbers of positions planned for study that served as the basis for projected savings between 1997 and 2003, which included studies in one service that began as early as 1993. Therefore, while the 1999 FYDP material lists studies of approximately 214,000 positions, our discussions with DOD components identified over 225,000 positions either already competed, under study, or planned for competition. We also obtained information on unrecognized costs, such as separation costs, from the Air Force's and the Navy's comptroller's offices, as well as the Army's Office of Program Analysis and Evaluation. We did not determine the reliability of the cost information provided by these offices. We met with officials from the Center for Naval Analyses to discuss their work on competitive sourcing within DOD, and obtained copies of their reports. We also spoke with responsible OSD, service, and installation officials, including manpower, contracting, and financial management officials to obtain information on the personnel resources required to conduct the studies and their ongoing efforts to reform their commercial activities databases.

To determine the extent to which uncertainties exist about meeting study goals and savings targets in the projected time frames, we met with responsible officials from OSD, the Army, the Air Force, the Navy, and the Marine Corps and contacted officials from defense agencies and installations. We obtained documentation on past, ongoing, and planned A-76 studies.

To evaluate the adequacy of the advance planning to support the effort underway, we met with representatives of the Defense Management Council and the A-76 Task Force, as well as cognizant service officials, to discuss their oversight role and the program implementation risks. We also researched relevant laws cited by officials.

We performed much of our work in Washington, D.C. However, we also conducted work at the Air Force Air Education and Training Command, San Antonio, Texas; the U.S. Army Training and Doctrine Command, Fort Monroe, Virginia; and the Naval Air Systems Command, Patuxet River, Maryland.

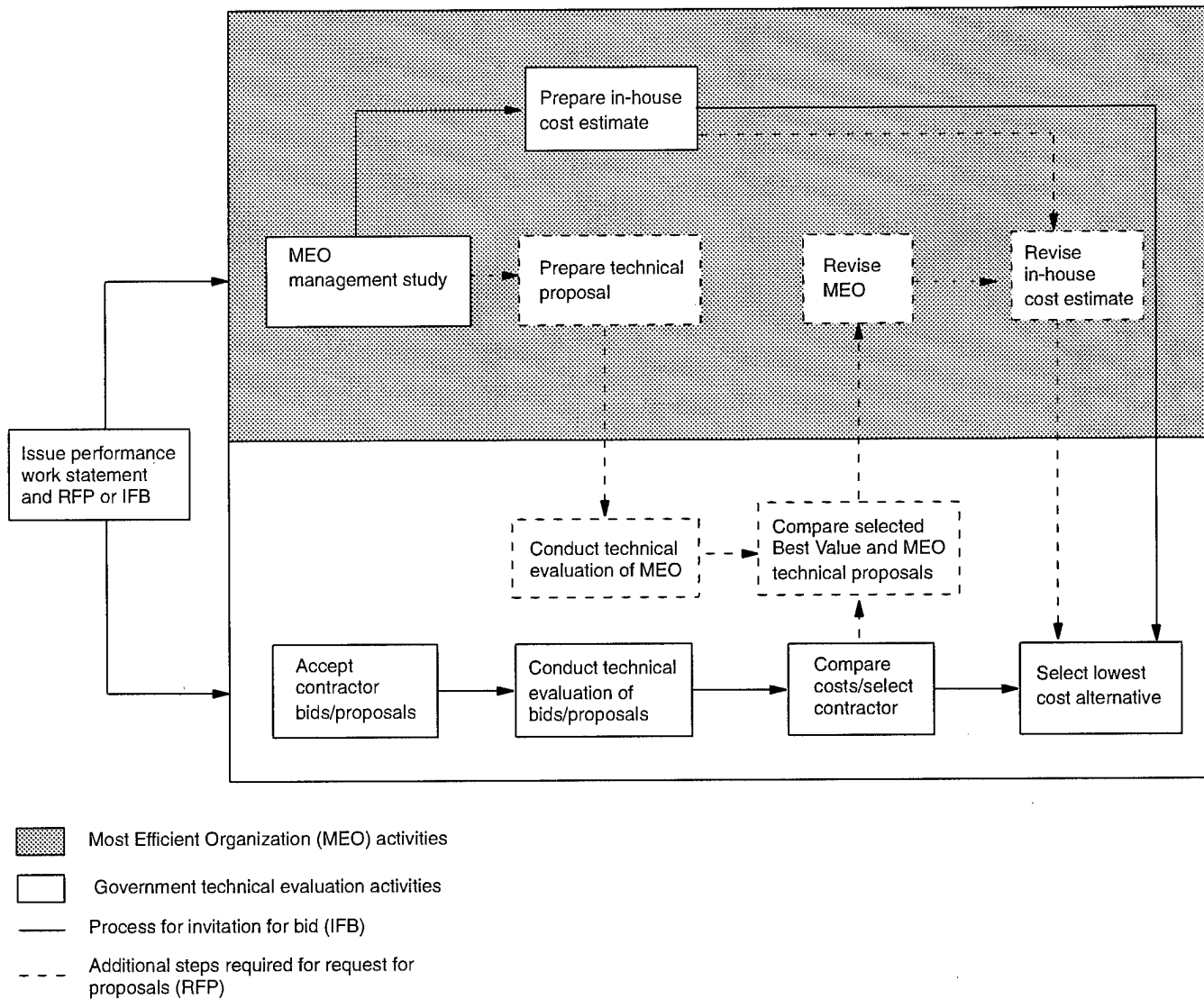
We conducted our review from September 1997 to December 1998 in accordance with generally accepted government auditing standards.

The A-76 Process

In general, the A-76 process consists of six key activities—(1) developing a performance work statement and quality assurance surveillance plan; (2) conducting a management study to determine the government's most efficient organization (MEO); (3) developing an in-house government cost estimate for MEO; (4) issuing a Request for Proposals or Invitation for Bid; (5) evaluating the proposals or bids and comparing the in-house estimate with a private sector offer or interservice support agreement and selecting the winner of the cost comparison; and (6) addressing any appeals submitted under the administrative appeals process, which is designed to ensure that all costs are fair, accurate, and calculated in the manner prescribed by the A-76 handbook.

Figure II.1 shows an overview of the process. The solid lines indicate the process used when the government issues an Invitation for Bids, requesting firm bids on the cost of performing a commercial activity. This type of process is normally used for more routine commercial activities, such as grass-cutting or cafeteria operations, where the work process and requirements are well defined. The dotted lines indicate the additional steps that take place when the government wants to pursue a negotiated, "best value" procurement. While it may not be appropriate for use in all cases, this type of process is often used when the commercial activity involves high levels of complexity, expertise, and risk.

Figure II.1: Overview of the A-76 Process



Source: Air Force Air Education and Training Command documents.

The circular requires the government to develop a performance work statement. This statement, which is incorporated into either the Invitation

for Bids or Request for Proposals, serves as the basis for both government estimates and private sector offers. If the Invitation for Bids process is used, each private sector company develops and submits a bid, giving its firm price for performing the commercial activity. While this process is taking place, the government activity performs a management study to determine the most efficient and effective way of performing the activity with in-house staff. Based on this "most efficient organization," the government develops a cost estimate and submits it to the selecting authority. The selecting authority concurrently opens the government's estimate along with the bids of all private sector firms.

According to OMB's A-76 guidance, the government's in-house estimate wins the competition unless the private sector's offer meets a threshold of savings that is at least 10 percent of direct personnel costs or \$10 million over the performance period. This minimum cost differential was established by the Office of Management and Budget (OMB) to ensure that the government would not contract out for marginal estimated savings.

If the Request for Proposals—best value process—is used, the Federal Procurement Regulation and the A-76 supplemental handbook require several additional steps. The private sector offerors submit proposals that often include a technical performance proposal and a price. The government prepares an in-house management plan and cost estimate based strictly on the performance work statement. On the other hand, private sector proposals can offer a higher level of performance or service.

The government's selection authority reviews the private sector proposals to determine which one represents the best overall value to the government based on such considerations as (1) higher performance levels, (2) lower proposal risk, (3) better past performance, and (4) cost to do the work. After the completion of this analysis, the selection authority prepares a written justification supporting its decision. This includes the basis for selecting a contractor other than the one that offered the lowest price to the government. Next, the authority evaluates the government's offer and determines whether it can achieve the same level of performance and quality as the selected private sector proposal. If not, the government must then make changes to meet the performance standards accepted by the authority. This ensures that the in-house cost estimate is based upon the same scope of work and performance levels as the best value private sector offer. After determining that the offers are based on the same level of performance, the cost estimates are compared. As with the Invitation for Bids process, the work will remain in-house unless the private offer is

Appendix II
The A-76 Process

(1) 10 percent less in direct personnel costs or (2) \$10 million less over the performance period.

Participants in the process—for either the Invitation for Bids or Request for Proposals process—may appeal the selection authority's decision if they believe the costs submitted by one or more of the participants were not fair, accurate, or calculated in the manner prescribed by the A-76 handbook.

Comments From the Department of Defense



ACQUISITION AND
TECHNOLOGY

OFFICE OF THE UNDER SECRETARY OF DEFENSE

3000 DEFENSE PENTAGON
WASHINGTON DC 20301-3000

February 16, 1999



Mr. David Warren
Director, Defense Management Issues
National Security and International Affairs Division
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Warren:

The Department of Defense (DoD) has reviewed the General Accounting Office (GAO) Draft Report, "DoD Competitive Sourcing: Questions About Goals, Pace and Risks of Key Reform Initiative," Dated December 23, 1998 (GAO Code 709300/OSD Case 1727). DoD concurs with the report's recommendations concerning the assessment of available resources to execute the Department's Competitive Sourcing Program and reexamination of its study targets, milestones and objectives.

Through internal reviews and program assessments, the Department identified the same concerns found in the GAO Draft Report. The Deputy Secretary proposed a number of initiatives that will make better use of our resources and improve efficiency in a December 9, 1998 memorandum to the Components. While it is accurate that some resources (mainly personnel to oversee the A-76 program) are diverted to accomplish the program, our objective is to limit the resource impact on local Commanders executing the program. Through the program and budget review process, the Department reviews the competitive sourcing study targets, milestones and objectives of the program to measure advancement towards our goals. Program adjustments are made as necessary. The Department has developed an aggressive competitive sourcing program by planning to compete nearly 229,000 positions by Fiscal Year 2005. We acknowledge that our program is met by a number of challenges, however, we believe none of these challenges are insurmountable. Components have not completed enough studies since FY 1997 to establish a baseline that would necessitate the reevaluation of our milestones and objectives. We expect as more studies are conducted that the Department will be able to better refine and adjust our study and savings objectives. Technical and administrative comments are enclosed.

Thank you for the opportunity to comment on the Draft Report.

Sincerely,

Randall A. Yim
Acting Deputy Under Secretary
(Installations)

Enclosure



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Appendix IV
Major Contributors to This Report

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Related GAO Products

OMB Circular A-76: Oversight and Implementation Issues (GAO/T-GGD-98-146, June 4, 1998).

Quadrennial Defense Review: Some Personnel Cuts and Associated Savings May Not Be Achieved (GAO/NSIAD-98-100, Apr. 30, 1998).

Competitive Contracting: Information Related to the Redrafts of the Freedom From Government Competition Act (GAO/GGD/NSIAD-98-167R, Apr. 27, 1998).

Defense Outsourcing: Impact on Navy Sea-Shore Rotations (GAO/NSIAD-98-107, Apr. 21, 1998).

Defense Infrastructure: Challenges Facing DOD in Implementing Defense Reform Initiatives (GAO/T-NSIAD-98-115, Mar. 18, 1998).

Defense Management: Challenges Facing DOD in Implementing Defense Reform Initiatives (GAO/T-NSIAD/AIMD-98-122, Mar. 13, 1998).

Base Operations: DOD's Use of Single Contracts for Multiple Support Services (GAO/NSIAD-98-83, Feb. 27, 1998).

Defense Outsourcing: Better Data Needed to Support Overhead Rates for A-76 Studies (GAO/NSIAD-98-62, Feb. 27, 1998).

Outsourcing DOD Logistics: Savings Achievable But Defense Science Board's Projections Are Overstated (GAO/NSIAD-98-48, Dec. 8, 1997).

Financial Management: Outsourcing of Finance and Accounting Functions (GAO/AIMD/NSIAD-98-43, Oct. 17, 1997).

Base Operations: Contracting for Firefighters and Security Guards (GAO/NSIAD-97-200BR, Sept. 12, 1997).

Terms Related to Privatization Activities and Processes (GAO/GGD-97-121, July 1997).

Defense Outsourcing: Challenges Facing DOD as It Attempts to Save Billions in Infrastructure Costs (GAO/T-NSIAD-97-110, Mar. 12, 1997).

Base Operations: Challenges Confronting DOD as It Renews Emphasis on Outsourcing (GAO/NSIAD-97-86, Mar. 11, 1997).

Related GAO Products

Public-Private Mix: Effectiveness and Performance of GSA's In-House and Contracted Services (GAO/GGD-95-204, Sept. 29, 1995).

Government Contractors: An Overview of the Federal Contracting-Out Program (GAO/T-GGD-95-131, Mar. 29, 1995).

Government Contractors: Are Service Contractors Performing Inherently Governmental Functions (GAO/GGD-92-11, Nov. 18, 1991).

OMB Circular A-76: Legislation Has Curbed Many Cost Studies in Military Services (GAO/GGD-91-100, July 30, 1991).

OMB Circular A-76: DOD's Reported Savings Figures Are Incomplete and Inaccurate (GAO/GGD-90-58, Mar. 15, 1990).

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